

Orange County Property Tax Story by the Numbers

The Governor signed AB 701, which was approved in the Legislature on September 12th, for what the press has termed the \$73M property tax dispute. If you happen to reside outside Orange County, the story linked below does have a bit of historical relevance for you regarding Proposition 13 (ruling property tax Constitutional Amendment of 1978) and the politics that helped Governor Jerry Brown and then Speaker Willie Brown set a formula in place that continues to impact, for better or worse, all counties today.

While Orange County must repay \$148M and give up \$50M granted in 2009, to garner \$53M, the deal reached between the County and State, understanding the issue and history, could be a win for Orange County, and a step in the right direction for the State.

2013 Legislation:

It is important to note that the County was/is at the mercy of the state, due to a recent court ruling on the 2 year struggle between the County and the State. Without getting into details, that are outlined below, the County argued for “parity” with other counties, the state argued that the County could not withhold funds. The State won on the first round. While parity with other counties is a sound argument, it has not yet prevailed, and may not on appeal. However, there could be an opportunity to negotiate in future years:

1. **Restores Property Tax Allocation.** Property Tax swap/adjustment in 2004 for all counties was \$1.00 of Property Tax for \$1.00 of Vehicles License Fees, except Orange County that received only \$0.76 for every \$1.00. (The adjustment was termed VLF-AA not to be confused with Vehicle License Fees or VLF.) The withholding of the funds is related to restructuring of Orange County debt after the 1994 bankruptcy reorganization (State did not bail out the County as explained below).
 - The restoration of \$0.24 for every \$1.00 is not at the \$76 million level the county desired for 2013-14 (dollar for dollar parity with other counties, as if the 2004 swap had not transpired) but at \$50M plus property tax growth, or roughly \$53M. Growth is projected at roughly 2% per year going forward.
2. **Allows longer than 3 years to repay the \$148 million owed the State.** \$148M is the equivalent of two years of the 2004 adjusted property taxes, withheld by the county during litigation. These funds have prudently remained in county reserves pending court ruling and therefore should not affect day-to-day operations.
 - Extension allows for general fund and cash-flow flexibility. The state extended the statutory 3 year pay back to 5 years, interest free: \$5M in 2014-15; \$15M in 2015-16; \$25M in 2016-17; \$50M and \$55M in 2016-17 and 2017-18 respectively.
3. **Takes Back \$50M negotiated by Correa in 2009 (SB 8) budget deal.** This represents a swap for the \$50M plus growth noted in #1 above. SB 8 does not grow.

The Continuing Dispute: In an attempt to explain the much misunderstood Orange County Property tax dispute with the state its best to understand the history surrounding the issue beginning in 1979:

After the passage of Proposition 13 in 1978, when to voters rebelled against out of control escalation in property taxes, then Governor Brown (yes, the same but younger) and Speaker Willie Brown, set about finding a formula to allocate property taxes within counties. Orange County, especially in the south, was relatively undeveloped and was somewhat agricultural or rural, and as such had few county services. The county was also seen as the catalyst for the passage of Proposition 13, and some believe that too was considered in setting the formula. With little exception, the 1979 formula remains in place today.

Below is a selection of coastal and similar counties statewide for comparison purposes:

% of Property Tax Allocation (based on 1979 formula)
Source: State Board of Equalization Annual Report 2010-11 Table 15

County	% County	% City	%School	% Other Districts	Population - 2011
Contra Costa	0.12	0.08	0.52	0.29	1,056,306
Los Angeles	0.20	0.14	0.47	0.18	9,847,712
San Diego	0.13	0.12	0.62	0.14	3,115,810
San Francisco	0.59	0.00	0.30	0.40	808,768
Ventura	0.16	0.08	0.53	0.24	827,874
San Mateo	0.13	0.10	0.61	0.13	722,372
Orange	0.06	0.10	0.62	0.22	3,028,846

The graph points out vividly the small percentage of property taxes the county retains compared to other similar counties. ***It is important to note that only School funding is backfilled by the state, so a lower percentage to schools does not affect education funding, but could greatly increase overall dollars to the county.***

While related to the 1979 formula, the dispute (that began two years ago) stems from a 2004 Schwarzenegger budget “swap” with cities and counties. Governor Brown in essence un-wrapped the 2004 “swap” of Vehicle License Fees for Property Tax Dollars with the 2011 Realignment. (Recall the Governor chose to implement Prison/Public Safety Realignment transferring dollars from the state to Counties.)

The Orange County dispute is unrelated to the policy of Realignment, but it's safe to say, had Realignment not occurred, the dispute would never have happened. To explain, the timeline below sets forth important milestones in the debate and dispute:

1. 1979 - 6% County allocation established after passage of Prop 13. (Average 58 counties: 10%) County/Cities in OC have since augmented with Home Owners Associations, Mello-Roos and other assessments.
2. 1994 - OC files for bankruptcy reorganization due to temp cash flow shortage created by derivative loss. Debt was restructured, state did not "bail-out" the County. But to insulate the state and municipalities from a credit downgrade, banks desire "collateral" of Vehicle License Fees vs. County Property Taxes. State and County agree to "swap" \$50M (+/-) in County Property Taxes for State VLF.
3. 2004 - Allocation adjusted with SB 1096 to allow 57 counties to SWAP \$1.00 of Vehicle License Fees for Property Taxes. Orange County agrees to receive \$0.76 (76 cents) in lieu of \$1.00 due to VLF guarantee for 1994 bond debt. The remaining 0.24 (24 cents) remains in VLF for debt repayment.
4. 2009 - Correa (AB 8) 2009 obtains a budget increase of \$35-\$50M of property taxes for restricted uses (Funds come from school allocation; recall state backfills schools.)
5. 2011 - Realignment sweeps VLF funds including 24 cents out of every property tax dollar allocated in OC for debt repayment. County received no benefit in Realignment allocation but penalty in Property Tax allocation. Due to increase in actual Property Tax revenues over projected, schools received an additional \$75M from county (recall school allocation is backfilled by state. If property taxes come in higher than projected, funds go to Education Reserve Augmentation Fund or ERAF). Adjustment was requested by the County, legislation was drafted, passed out of the Assembly, but do to delays, was never voted on in the Senate. Unfortunately, adjustment could have been made at that time saving legal wrangling, however, the issue was being confused with VLF for overall Prison Realignment.

Actual funds swapped for debt repayment were \$50M, but County withheld roughly \$73M from state based on what would have been allowed if Orange County had been treated with parity to other counties in the 2004 swap. (County withheld \$148M over 2 years pending litigation.)

State sues county, and state wins on procedure rather than policy in 2013. Court rules County cannot withhold funds from state regardless of parity claims. State and county enter negotiations for repayment which was mandated by the court.

To conclude, legislation passed both houses September 12th and, signed by the Governor, given the circumstances, the Orange County Legislative Delegation, the Governor and the County Supervisors have struck a workable solution to begin mending past wounds, keeping the county budget balanced, reserves in place and flexibility for Supervisors present and future. Considering the State could have demanded the \$148M over three years, taken the Correa \$50M and refused to allow the roughly \$53M adjustment, the deal is a win for the OC, and appears to be a step in the right direction for the state.